HOME PROPERTIES INC
Form 10-Q
May 02, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2014

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ____________________ to ____________________

Commission File Number: 1-13136

HOME PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

MARYLAND	16-1455126
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
850 Clinton Square, Rochester, New York	14604
(Address of principal executive offices)	(Zip Code)

(585) 546-4900

(Registrant s telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes þ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common Stock	Outstanding at April 23, 2014
$.01 par value	57,131,393

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HOME PROPERTIES, INC.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HOME PROPERTIES, INC.

CONSOLIDATED BALANCE SHEETS

MARCH 31, 2014 AND DECEMBER 31, 2013

(Dollars in thousands, except per share data)

(Unaudited)

	March 31, 2014	December 31, 2013
ASSETS		
Real estate:		
Land	$ 770,851	$ 786,868
Construction in progress	192,111	187,976
Buildings, improvements and equipment	4,588,065	4,645,921
	5,551,027	5,620,765
Less: accumulated depreciation	(1,258,186)	(1,243,243)
Real estate, net	4,292,841	4,377,522
Cash and cash equivalents	8,403	9,853
Cash in escrows	26,006	23,738
Accounts receivable, net	15,118	14,937
Prepaid expenses	15,777	22,089
Deferred charges, net	11,021	11,945
Other assets	7,059	7,793
Total assets	$ 4,376,225	$4,467,877
LIABILITIES AND EQUITY		
Mortgage notes payable	$ 1,725,359	$1,814,217
Unsecured notes payable	450,000	450,000
Unsecured line of credit	179,000	193,000
Accounts payable	28,193	27,540
Accrued interest payable	10,362	8,392
Accrued expenses and other liabilities	31,097	33,936
Security deposits	18,310	18,479
Total liabilities	2,442,321	2,545,564
Commitments and contingencies		
Equity:		
Preferred stock, $0.01 par value; 10,000,000 shares authorized; no shares issued or outstanding	-	-
Common stock, $0.01 par value; 80,000,000 shares authorized; 57,106,862 and 56,961,646 shares issued and outstanding at March 31, 2014 and December 31, 2013, respectively	571	570

Excess stock, $0.01 par value; 10,000,000 shares authorized; no shares issued or outstanding	-	-
Additional paid-in capital	2,016,474	2,007,300
Distributions in excess of accumulated earnings	(376,159)	(380,168)
Accumulated other comprehensive income	792	1,551
Total common stockholders equity	1,641,678	1,629,253
Noncontrolling interest	292,226	293,060
Total equity	1,933,904	1,922,313
Total liabilities and equity	$ 4,376,225	$4,467,877

The accompanying notes are an integral part of these consolidated financial statements.

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HOME PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands, except per share data)

(Unaudited)

	Three months ended March 31, 2014	2013
Revenues:		
Rental income	$ 152,354	$ 147,293
Property other income	15,560	14,181
Other income	141	249
Total revenues	168,055	161,723
Expenses:		
Operating and maintenance	66,459	60,057
General and administrative	9,258	9,083
Interest	25,327	29,995
Depreciation and amortization	44,378	41,412
Other expenses	8	17
Total expenses	145,430	140,564
Income from continuing operations	22,625	21,159
Discontinued operations:		
Income from discontinued operations	40	808
Gain on disposition of property	31,306	40,359
Discontinued operations	31,346	41,167
Net income	53,971	62,326
Net income attributable to noncontrolling interest	(8,180)	(10,446)
Net income attributable to common stockholders	$ 45,791	$ 51,880
Basic earnings per share:		
Income from continuing operations	$ 0.34	$ 0.34
Discontinued operations	0.46	0.67
Net income attributable to common stockholders	$ 0.80	$ 1.01
Diluted earnings per share:		
Income from continuing operations	$ 0.33	$ 0.34
Discontinued operations	0.46	0.65
Net income attributable to common stockholders	$ 0.79	$ 0.99
Weighted average number of shares outstanding:		
Basic	57,106,853	51,618,734
Diluted	57,620,655	52,325,410

The accompanying notes are an integral part of these consolidated financial statements.

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HOME PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

(Unaudited)

	Three months ended March 31, 2014	Three months ended March 31, 2013
Net income	$ 53,971	$ 62,326
Other comprehensive income (loss):		
Unrealized gain (loss) on interest rate swap agreements	(895)	212
Other comprehensive income (loss)	(895)	212
Comprehensive income	53,076	62,538
Net income attributable to noncontrolling interest	(8,180)	(10,446)
Other comprehensive (income) loss attributable to noncontrolling interest	136	(35)
Comprehensive income attributable to common stockholders	$ 45,032	$ 52,057

The accompanying notes are an integral part of these consolidated financial statements.

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HOME PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF EQUITY

FOR THE THREE MONTHS ENDED MARCH 31, 2014 AND THE YEAR ENDED DECEMBER 31, 2013

(Dollars in thousands)

(Unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Distributions in Excess of Accumulated Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total
Balance, January 1, 2013	51,508,142	$ 515	$ 1,709,919	$(388,397)	$ (1,069)	$ 267,299	$ 1,588,267
Net income	-	-	-	160,873	-	30,706	191,579
Unrealized gain (loss) on interest rate swap agreements	-	-	-	-	2,620	516	3,136
Issuance of common stock, net	902,934	9	47,477	-	-	-	47,486
Issuance of common stock through public offering, net	4,427,500	44	267,589	-	-	-	267,633
Stock-based compensation	3,137	-	9,055	-	-	-	9,055
Repurchase of common stock	(48,484)	-	(3,133)	-	-	-	(3,133)
Conversion of UPREIT Units for common stock	168,417	2	4,493	-	-	(4,495)	0
Adjustment of noncontrolling interest	-	-	(28,100)	-	-	28,100	0
Dividends and distributions paid	-	-	-	(152,644)	-	(29,066)	(181,710)
Balance, December 31, 2013	56,961,646	$ 570	$ 2,007,300	$(380,168)	$ 1,551	$ 293,060	$ 1,922,313
Net income	-	-	-	45,791	-	8,180	53,971
Unrealized gain (loss) on interest rate swap agreements	-	-	-	-	(759)	(136)	(895)
Issuance of common stock, net	81,952	1	3,180	-	-	-	3,181
Stock-based compensation	2,990	-	5,064	-		-	5,064
Repurchase of common stock	(8,449)	-	(484)	-	-	-	(484)
Conversion of UPREIT Units for common stock	68,723	-	1,957	-	-	(1,957)	0
Adjustment of noncontrolling interest	-	-	(543)	-	-	543	0
Dividends and distributions paid	-	-	-	(41,782)	-	(7,464)	(49,246)
Balance, March 31, 2014	57,106,862	$ 571	$ 2,016,474	$ (376,159)	$ 792	$ 292,226	$ 1,933,904

The accompanying notes are an integral part of these consolidated financial statements.

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HOME PROPERTIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE THREE MONTHS ENDED MARCH 31, 2014 AND 2013

(Dollars in thousands)

(Unaudited)

	2014	2013
Cash flows from operating activities:		
Net income	$ 53,971	$ 62,326
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	45,619	44,098
Gain on disposition of property	(31,306)	(40,359)
Stock-based compensation	5,064	4,327
Changes in assets and liabilities:		
Cash in escrows, net	(2,271)	(2,932)
Other assets	6,100	3,481
Accounts payable and accrued liabilities	1,305	4,713
Total adjustments	24,511	13,328
Net cash provided by operating activities	78,482	75,654
Cash flows from investing activities:		
Purchase of land for development	-	(28,088)
Capital improvements to properties including redevelopment	(24,059)	(27,072)
Additions to construction in progress	(12,321)	(19,124)
Additions to predevelopment	(509)	(78)
Proceeds from sale of properties, net	106,273	106,158
Proceeds from insurance for property losses	88	-
Withdrawals from (additions to) cash held in escrow, net	3	(4,615)
Net cash provided by investing activities	69,475	27,181
Cash flows from financing activities:		
Proceeds from sale of common stock, net	3,181	31,693
Repurchase of common stock	(484)	(241)
Scheduled payments of mortgage notes payable	(8,124)	(9,082)
Payoff mortgage notes payable	(80,734)	(101,020)
Proceeds from unsecured line of credit	112,000	170,500
Payments on unsecured line of credit	(126,000)	(164,000)
Withdrawals from cash held in escrow, net	-	(227)
Dividends and distributions paid	(49,246)	(43,460)
Net cash used in financing activities	(149,407)	(115,837)
Net decrease in cash and cash equivalents	(1,450)	(13,002)
Cash and cash equivalents:		
Beginning of year	9,853	21,092
End of period	$ 8,403	$ 8,090

Supplemental disclosure:

Interest capitalized	$ 2,169	$ 1,578
Supplemental disclosure of non-cash investing and financing activities:		
Exchange of UPREIT Units for common shares	1,957	1,138
Transfers of construction in progress to buildings, improvements and equipment	7,878	96
Capital improvements to properties and construction in progress included in accounts payable	4,961	4,054

The accompanying notes are an integral part of these consolidated financial statements.

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HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

1 ORGANIZATION AND BASIS OF PRESENTATION

Organization

Home Properties, Inc. (the Company) was formed in November 1993, as a Maryland corporation and is engaged in the ownership, management, acquisition, rehabilitation and development of residential apartment communities primarily in selected Northeast and Mid-Atlantic regions of the United States. The Company completed an initial public offering of 5,408,000 shares of common stock on August 4, 1994 and is traded on the New York Stock Exchange (NYSE) under the symbol HME . The Company is included in Standard & Poor s MidCap 400 Index.

The Company conducts its business through Home Properties, L.P. (the Operating Partnership), a New York limited partnership. As of March 31, 2014, the Company owned and operated 119 apartment communities with 41,532 apartments.

The Company has elected to be taxed as a real estate investment trust (REIT) under the Internal Revenue Code of 1986, as amended, commencing with the taxable year ended December 31, 1994. As a result, the Company generally is not subject to federal or state income taxation at the corporate level to the extent it distributes annually at least 90% of its REIT taxable income to its shareholders and satisfies certain other requirements. For all periods presented, the Company distributed in excess of 100% of its taxable income; accordingly, no provision has been made for federal income taxes in the accompanying consolidated financial statements.

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Company and its ownership of 84.9% of the limited partnership units in the Operating Partnership (UPREIT Units) at March 31, 2014 (84.8% at December 31, 2013). The remaining 15.1% is included as noncontrolling interest in these consolidated financial statements at March 31, 2014 (15.2% at December 31, 2013). The Company periodically adjusts the carrying value of noncontrolling interest to reflect its share of the book value of the Operating Partnership. Such adjustments are recorded to additional paid in capital as a reallocation of noncontrolling interest in the accompanying consolidated statements of equity. The Company owns a 1.0% general partner interest in the Operating Partnership and the remainder indirectly as a limited partner through its wholly owned subsidiary, Home Properties I, LLC, which owns 100% of Home Properties Trust, which is the limited partner. Home Properties Trust was formed in September 1997, as a Maryland real estate trust and as a qualified REIT subsidiary (QRS), and owns the Company s share of the limited partner interests in the Operating Partnership.

The accompanying consolidated financial statements include the accounts of Home Properties Resident Services, Inc. (HPRS). HPRS is a wholly owned subsidiary of the Company. All significant inter-company balances and transactions have been eliminated in these consolidated financial statements.

The accompanying consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the applicable rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain disclosures that would accompany annual financial statements prepared in accordance with GAAP are omitted. The year-end December 31, 2013 balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. In the opinion of management, all adjustments, consisting solely of normal recurring adjustments, necessary for the fair statement of the consolidated financial statements for the interim periods have been included. The results of operations for the interim periods are not necessarily indicative of results which ultimately may be achieved for the full year. These interim consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Form 10-K for the year ended December 31, 2013. Certain reclassifications have been made to the 2013 financial statements to conform to the 2014 presentation as a result of discontinued operations.

HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

2 RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING STANDARDS

On April 10, 2014, the Financial Accounting Standards Board (FASB) issued ASC 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity,* which raises the threshold for determining which disposals are required to be presented as discontinued operations and modifies related disclosure requirements. The standard is applied prospectively and is effective in 2015 with early adoption permitted. The Company is currently assessing the potential impact that the adoption of this guidance will have on its financial position and results of operations.

3 DEVELOPMENT

Redevelopment

The Company has one project under redevelopment. Arbor Park, located in Alexandria, Virginia, has 851 garden apartments in fifty-two buildings built in 1967. The Company is part way through a project to extensively renovate all of the units over several years on a building by building basis. As of March 31, 2014, there was one building with 36 units under renovation and forty buildings with 638 units completed and 522 of those units occupied. As of March 31, 2014, the Company has incurred costs of $23,200 for the renovation which is included in buildings, improvements and equipment. The entire project is expected to be completed in 2015.

Development

During the fourth quarter of 2011, the Company started construction on Eleven55 Ripley, located in Silver Spring, Maryland, consisting of two buildings, a 21 story high-rise and a 5 story mid-rise, for a total of 379 apartment units. Initial occupancy occurred in the fourth quarter of 2013. Construction is expected to be completed in the third quarter of 2014. The construction in progress for this development was $94,172 as of March 31, 2014.

During the second quarter of 2012, the Company started construction on The Courts at Spring Mill Station, located in Conshohocken, Pennsylvania, a suburb of Philadelphia. The combination donut/podium style project, consisting of two buildings, will have a total of 385 apartment units. Construction is expected to be completed in the second half of 2014 with initial occupancy in the third quarter of 2014. The construction in progress for this development was $48,419 as of March 31, 2014.

During the first quarter of 2013, the Company purchased a land parcel located in Tysons Corner, Virginia. The Company intends to develop approximately 694 units in a residential community on this entitled parcel. The construction in progress for this development, consisting primarily of land value, was $34,627 as of March 31, 2014.

During the fourth quarter of 2013, the Company purchased a land parcel located in Linthicum, Maryland, a suburb of Baltimore. The land is intended for future development of approximately 300 multifamily units. The construction in progress for this development, consisting primarily of land value, was $14,893 as of March 31, 2014.

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HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

4 UNSECURED NOTES PAYABLE

Unsecured Term Loan

In December 2011, the Company entered into a five-year unsecured term loan for $250,000 with M&T Bank as lead bank, and ten other participating lenders, which was set to mature on December 8, 2016. On August 19, 2013, the Company amended the loan agreement to extend the maturity date to August 18, 2018. No other changes were made to the terms of the unsecured term loan. The loan bears monthly interest at a variable rate based on LIBOR, plus a spread from 1.00% to 2.00% based on the Company s leverage ratio. The unsecured term loan has covenants that align with the unsecured line of credit facility described in Note 5. The Company was in compliance with these financial covenants for all periods presented.

On July 19, 2012, the Company entered into two interest rate swap agreements that effectively convert the variable LIBOR portion of this loan to a fixed rate of 0.685% through December 7, 2016. On November 4, 2013, the Company entered into three additional interest rate swap agreements that effectively convert the variable LIBOR portion of this loan to a fixed rate of 2.604% for the period of December 8, 2016 through August 18, 2018. The interest rate swap agreements are more fully described in Note 7. As of March 31, 2014, based on the Company s leverage ratio, the spread was 1.00%, and the one-month LIBOR was swapped at 0.685%; resulting in an effective rate of 1.685% for the Company.

Unsecured Senior Notes

In December 2011, the Company issued $150,000 of unsecured senior notes. The notes were offered in a private placement in two series: Series A: $90,000 with a seven-year term due December 19, 2018 at a fixed interest rate of 4.46% (Series A); and, Series B: $60,000 with a ten-year term due December 19, 2021 at a fixed interest rate of 5.00% (Series B).

On June 27, 2012, the Company issued another private placement note in the amount of $50,000 with a seven-year term, a fixed rate of 4.16% and a June 27, 2019 due date. The proceeds from this note were used to partially fund the purchase of a 1,350 unit apartment community on June 28, 2012.

The unsecured senior notes are subject to various covenants and maintenance of certain financial ratios. Although the covenants of the notes do not duplicate all the covenants of the unsecured line of credit facility, any covenants applicable to both the notes and the line are identical. The Company was in compliance with these financial covenants for all periods presented.

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HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

5 UNSECURED LINE OF CREDIT

On August 19, 2013, the Company entered into a First Amendment to the Amended and Restated Credit Agreement (the Credit Agreement), which provides for a $450,000 revolving credit facility with an initial maturity date of August 18, 2017 and a one-year extension at the Company s option. The Credit Agreement amended the Company s prior $275,000 facility, which was scheduled to expire on December 8, 2015, not including a one-year extension at the Company s option. The Credit Agreement is with M&T Bank and U.S. Bank National Association as joint lead arrangers, M&T Bank as administrative agent and nine other commercial banks as participants. The Company had $179,000 outstanding under the credit facility as of March 31, 2014. Borrowings under the line of credit bear interest at a variable rate based on LIBOR, plus a spread from 1.00% to 2.00% based on the Company s leverage ratio. As of March 31, 2014, based on the Company s leverage ratio, the spread was 1.00%, and the one-month LIBOR was 0.19%; resulting in an effective rate of 1.19% for the Company.

The Credit Agreement requires the Company to maintain certain financial ratios and measurements including a limitation on outstanding indebtedness and a minimum interest coverage ratio. The Company was in compliance with these financial covenants for all periods presented.

The Credit Agreement also provides the ability to issue up to $20,000 in letters of credit. While the issuance of letters of credit does not increase borrowings outstanding under the line of credit, it does reduce the amount available. At March 31, 2014, the Company had outstanding letters of credit of $5,237 and the amount available on the credit facility was $265,763.

6 FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial Instruments Carried at Fair Value

The fair value of interest rate swaps, which are more fully described in Note 7, are determined using the market standard of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The variable cash payments (or receipts) are based on an expectation of future interest rate forward curves derived from observable market interest rate curves (level 2 inputs, as defined by the authoritative guidance). The Company incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty s nonperformance risk in the fair value measurements. The Company has determined that the significant inputs used in this model are observable in active markets, therefore considers the interest rate swap asset valuation of $945 at March 31, 2014 and the asset valuation of $1,840 at December 31, 2013 as level 2 classifications within the fair value hierarchy.

Financial Instruments Not Carried at Fair Value

The Company follows the authoritative guidance for fair value measurements when valuing its financial instruments for disclosure purposes. The valuation of financial instruments requires the Company to make estimates and judgments that affect the fair value of the instruments.

Cash and cash equivalents, cash in escrows, accounts receivable, other assets, accounts payable, accrued interest payable, accrued expenses and other liabilities, except for interest rate swaps, are all carried at their face amounts, which approximate their fair values due to their relatively short-term nature and high probability of realization.

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HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

6 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Financial Instruments Not Carried at Fair Value (continued)

The Company determined the fair value of its mortgage notes payable, unsecured term loan, unsecured senior notes and unsecured line of credit facility using a discounted future cash flow technique that incorporates observable market-based inputs, including a market interest yield curve with adjustments for duration, loan to value (level 2 inputs), and risk profile (level 3 inputs). In determining the market interest yield curve, the Company considered its investment grade credit ratings (level 2 inputs). The Company has determined that the significant inputs used in this model are observable in active markets, therefore considers the valuation classified as level 2 of the fair value hierarchy. At March 31, 2014 and December 31, 2013, the fair value of the Company s total debt, consisting of the mortgage notes, the unsecured term loan, unsecured senior notes and unsecured line of credit, amounted to a liability of $2,465,531 and $2,552,145, respectively, compared to its carrying amount of $2,354,359 and $2,457,217, respectively.

7 DERIVATIVE AND HEDGING ACTIVITIES

Risk Management Objective of Using Derivatives

The Company s objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. The Company does not utilize these arrangements for trading or speculative purposes.

Cash Flow Hedges of Interest Rate Risk

On July 19, 2012, the Company entered into two interest rate swap agreements that effectively convert the one-month LIBOR portion of a $250,000 five-year variable rate unsecured term loan, originally due on December 8, 2016, from a variable rate of one-month LIBOR plus a spread of 1.00% to 2.00% based on the Company s leverage ratio to a fixed rate of 0.685% plus the applicable spread. As further described in Note 4, the $250,000 unsecured term loan was amended to extend the maturity date to August 18, 2018. On November 4, 2013, the Company entered into three additional interest rate swap agreements for the period of December 8, 2016 through August 18, 2018 to succeed the original two swaps. These three forward swaps effectively convert the variable rate of one-month LIBOR plus a spread of 1.00% to 2.00% based on the Company s leverage ratio to a fixed rate of 2.604% plus the applicable spread.

As of March 31, 2014, the Company had the following outstanding interest rate derivatives that were designated as cash flow hedges of interest rate risk:

Interest Rate Derivative	Notional Amount	Fixed Interest Rate	Variable Interest Rate	Effective Date	Maturity Date
Interest rate swap	$ 150,000	0.6800%	One-month LIBOR	August 13, 2012	December 8, 2016
Interest rate swap	$ 100,000	0.6925%	One-month LIBOR	August 13, 2012	December 8, 2016
Interest rate swap	$ 100,000	2.6010%	One-month LIBOR	December 8, 2016	August 18, 2018
Interest rate swap	$ 75,000	2.6010%	One-month LIBOR	December 8, 2016	August 18, 2018
Interest rate swap	$ 75,000	2.6125%	One-month LIBOR	December 8, 2016	August 18, 2018

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HOME PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

7 DERIVATIVE AND HEDGING ACTIVITIES (continued)

Cash Flow Hedges of Interest Rate Risk (continued)

The table below presents the fair value of the Company s derivative financial instruments as well as their classification on the balance sheets as of March 31, 2014 and December 31, 2013:

Fair Value of Derivative Instruments

	Asset Derivatives			Liability Derivatives		
	Balance	Fair Value at		Balance	Fair Value at	
	Sheet Location	3/31/2014	12/31/2013	Sheet Location	3/31/2014	12/31/2013
Interest Rate Swap	Other Assets	$ 945	$ 1,840	Other Liabilities	$ -	$ -

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges are recorded in accumulated other comprehensive income and are subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. During 2014 and 2013, such derivatives were used to hedge the variable cash flows associated with certain variable-rate debt. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During the three months ended March 31, 2014 and 2013, the Company did not record any hedge ineffectiveness.

Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on the Company s variable-rate debt. The Company estimates that an additional $1,178 will be reclassified from accumulated other comprehensive income as an increase to interest expense over the next twelve months.

The table below details the location in the financial statements of the gain or loss recognized on interest rate derivatives designated as cash flow hedges for the three months ended March 31, 2014 and 2013, respectively:

	Three Months Ended March 31,